BUILDING A STRONGER FUTURE.

ANNUAL REPORT 2005

ENERCHEM
INTERNATIONAL INC.

Enerchem International Inc. is a manufacturer and distributor of hydrocarbon fluids providing solutions to oil and gas processing and production problems and is also a provider of energy marketing services. The Company's common shares trade on the Toronto Stock Exchange under the symbol "ECH".

Our Mission Statement

Enerchem strives to provide our customers with premium products, outstanding service and superior technical expertise in a safe and environmentally conscientious manner, while enhancing value to our shareholders. Our employees are committed to providing a culture that is based on sound business ethics, integrity, trust and core values that exceed industry standards.

Contents

Annual General Meeting

The Annual General Meeting of the Shareholders will be held on
Wednesday, May 17, 2006 at 10:00 am
At the Calgary Petroleum Club, Viking Room
319 – 5th Avenue S.W.
Calgary, Alberta, Canada

All shareholders are cordially invited to attend.

ENERCHEM
INTERNATIONAL INC.

Financial Highlights

Results of Operations

For the years ended December 31	2005	2004
	$	$
Revenues	109,132,279	63,619,257
Net earnings		
Continuing operations	3,884,508	759,654
Discontinued operations	4,290,230	1,201,046
Net earnings for the year	8,174,738	1,960,700
Basic earnings per share		
Continuing operations	0.26	0.05
Discontinued operations	0.29	0.09
Net earnings per share basic	0.55	0.14
Diluted earnings per share		
Continuing operations	0.26	0.05
Discontinued operations	0.29	0.08
Net earnings per share diluted	0.55	0.13
EBITDA (1)	6,974,289	2,775,881
EBITDA per share (2)	0.47	0.19

Financial Position

Total assets	73,921,005	61,653,226
Working capital (3)	23,553,974	11,432,960
Total long-term financial liabilities (4)	1,832,276	3,042,634
Shareholders' equity	48,224,692	39,206,314
Number of shares		
Outstanding, end of year	14,820,807	14,594,610
Average, during the year (5)	14,793,712	14,396,811

(1) represents earnings before interest, taxes, depreciation, amortization and accretion expense
(2) calculated as EBITDA divided by the basic weighted average number of shares outstanding during the year.
(3) calculated as current assets less current liabilities
(4) excludes current portion of long-term debt and obligations under capital leases
(5) represents the weighted basic average number of shares outstanding during the year

President's Message

To Our Shareholders,

On behalf of the Board of Directors of Enerchem International Inc. I am pleased to report the operational and financial results of the Company for the fourth quarter and year ended December 31, 2005.

2005 proved to be another year of unprecedented growth within the Western Canadian oil and gas industry. Energy prices continued to increase throughout 2005, which resulted in record drilling activity with almost 23,900 wells drilled by year-end. This brought about continued demand for our premium products and increased utilization of our fractionation plants. Despite some first quarter operational difficulties with our Slave Lake plant and less than pristine weather conditions in the second and third quarters, we have persistently risen to the challenge in this competitive market. Enerchem has remained a commercial leader by surpassing industry standards concerning product quality in our operating environment.

Each quarterly report of 2005 demonstrated significant increases in revenue, net earnings and earnings per share from the previous year. Revenues from continuing operations for the year ended December 31, 2005 increased by 72% to $109,132,000 from $63,619,000 in 2004. Earnings per share from continuing operations rose from $0.05 in 2004 to $0.26 by the end of 2005 and net earnings from continuing operations reached a record $3,885,000, an impressive 411% increase over 2004 earnings from continuing operations. With the sale of the specialty chemicals operations, total net earnings for 2005 increased by 316% to $8,175,000 from $1,961,000 last year. Overall, earnings per share were $0.55 in 2005 compared to $0.14 last year.

With industry expectations for 2006 projecting continued high levels of activity, we look forward to another successful year.

Shifting the Balance

Several operational issues that impeded growth in the past have been resolved. After a careful performance review of our services, capabilities and growth opportunities, we opted to refocus our capital and resources towards the expansion of our hydrocarbon fluids opportunities and energy marketing operations. As a result, plant and facility infrastructures utilized in the manufacture of our specialty chemical fluids were divested by year end.

Overall, throughout 2005 our plants in Slave Lake and Sundre continued to operate at higher rates of utilization and efficiencies as a result of novel improvements to their infrastructures. We have established a feedstock pipeline off-load that will expedite our access to light sweet crude and minimize crude quality issues. Furthermore, the implementation of additional tank storage in Slave Lake for feedstock and other vital products has supplemented productivity. We are also pleased with our growth in drilling fluids market share in 2005 and we are focused on initiatives that will assist to strengthen sales of our specialty fluids in 2006.

One of our major challenges over the last year pertained to internal transportation. In response, we have ordered additional trucking capacity to come on line during the first quarter of 2006. We will continue to develop our fleet throughout the coming year in order to meet our shipping requirements and further assist in the reduction of our transportation costs.

The first quarter of 2006 will also see the commissioning of a new refrigeration unit and the completion of additional infrastructure at the Slave Lake plant in order to provide additional flexibility for our energy marketing activities. We will also be completing a new flowback cleaning facility in order to recycle used frac fluid which will help to reduce crude oil feedstock purchases.

Outlook

With an expectation for commodity prices to remain high, this should continue to augment industry activity. Current forecasts estimate that over 25,000 wells will be drilled in 2006. This increase in drilling activity and more fracturing capacity being added throughout the deeper, more technical, areas of the Western Canadian Sedimentary Basin indicate the necessity of our services and an increasing need for our products for the foreseeable future.

Acknowledgements

I would like to sincerely thank our Board of Directors for their direction, our employees for their commitment, innovation and dedication, and our shareholders for their continued support.

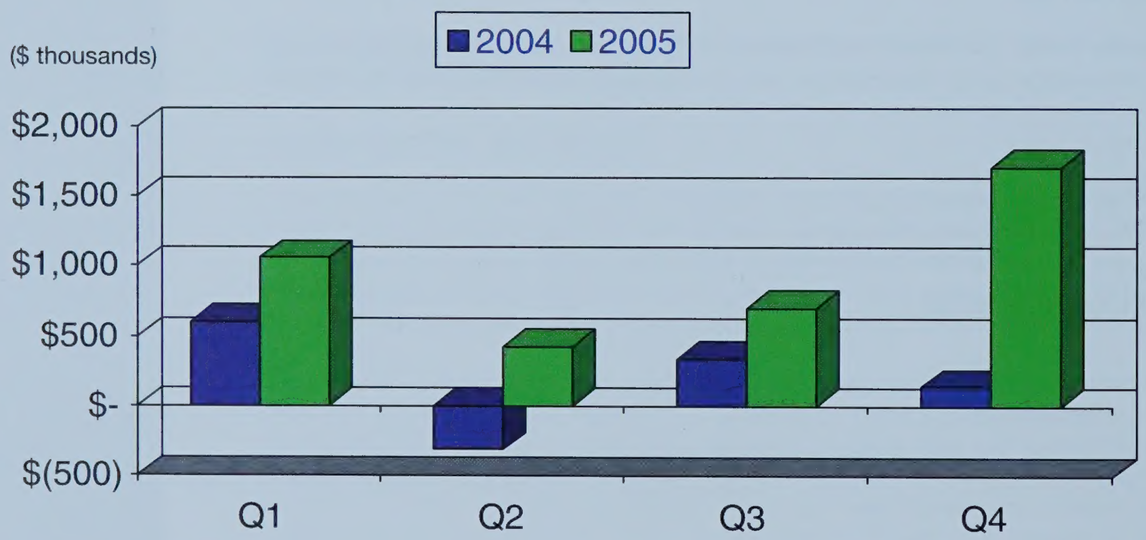
Douglas F. Robinson
President and Chief Executive Officer

Year in Review

Financial and Operating Highlights

- The highest earnings in the Company's history were achieved, $3.9 million and earnings per share of $0.26.
- Reliability of the Company's fractionation plants improved dramatically as feedstock and plant operational issues were actively managed in all areas under its direct control.
- The completion of the Slave Lake tank farm during the third quarter of 2005 marked a turning point by facilitating greater operational flexibility and by-product fluids management.
- Return on average capital employed improved to 13.5% in 2005 from 4.4% in 2004.

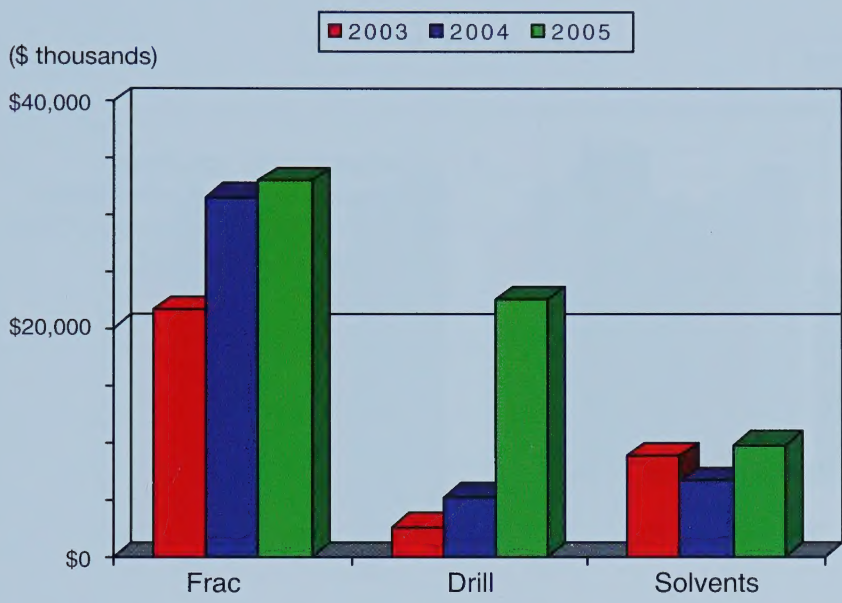
Net earnings from continuing operations by quarter



- Revenues and quarterly earnings improved throughout 2005 when compared to 2004.

Year in Review

Oilfield Services - Revenues



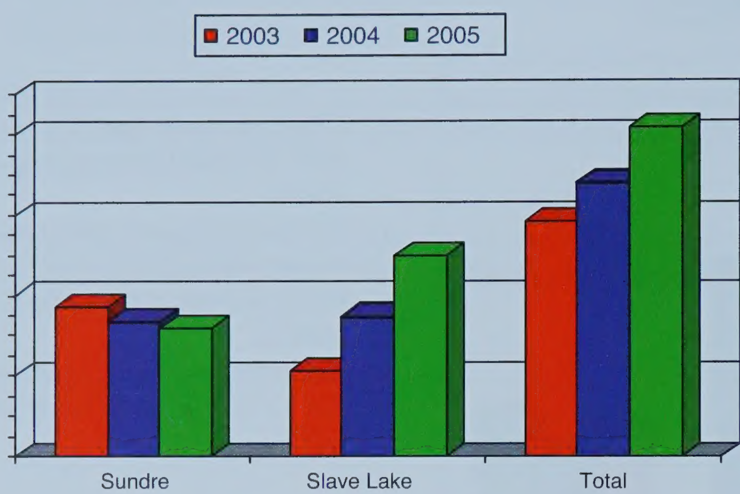
- Product revenues increased by 51% in 2005 when compared to 2004.
- Achieved record drilling fluid revenues in 2005 of $22.5 million.
- Fracturing fluid revenues of $33 million.
- Solvent revenues increased by 49% in 2005 when compared to 2004.

Energy Marketing - Revenues

- Started in Q3 2004.
- Provides opportunity to maximize by-product values.
- Net margin ranges from 10% to 15%.

Year in Review

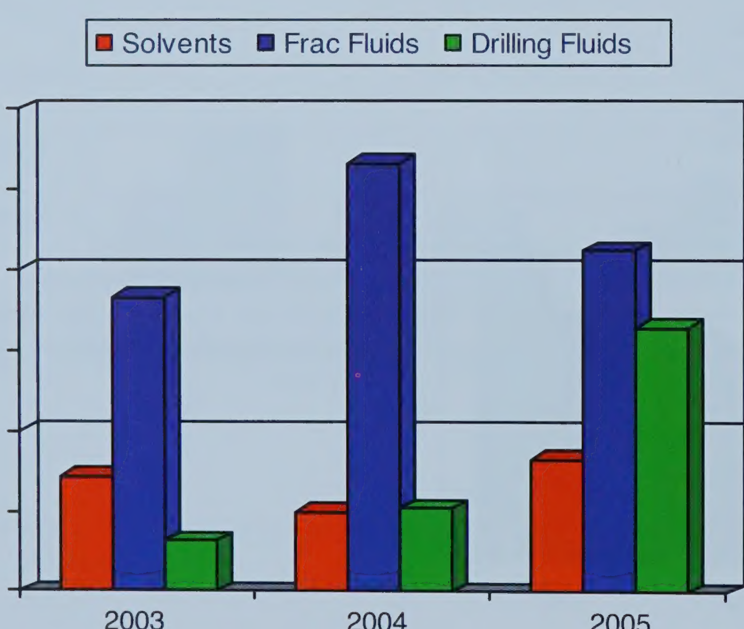
Feedstock Volumes



(relative scale)

- Total feedstock volumes processed by the fractionation plants in 2005 increased by 20% when compared to 2004.

Product Volumes

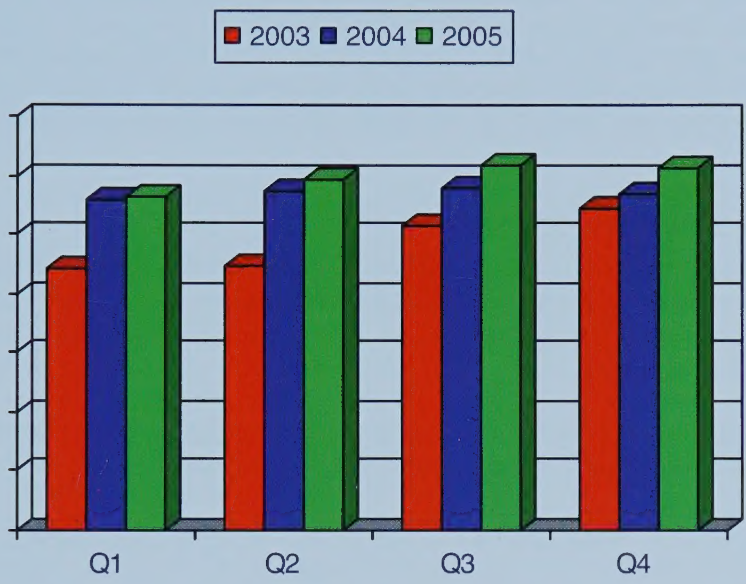


(relative scale)

- Overall, total volume of product sold in 2005 increased by 13% when compared to 2004.
- Fracturing fluid volumes declined in 2005 largely as a result of feedstock quality issues during the first quarter 2005.
- Drilling fluid volumes increased by 223% in 2005 when compared to 2004.
- Solvent fluid volumes increased by 41% from 2004 levels.

Year in Review

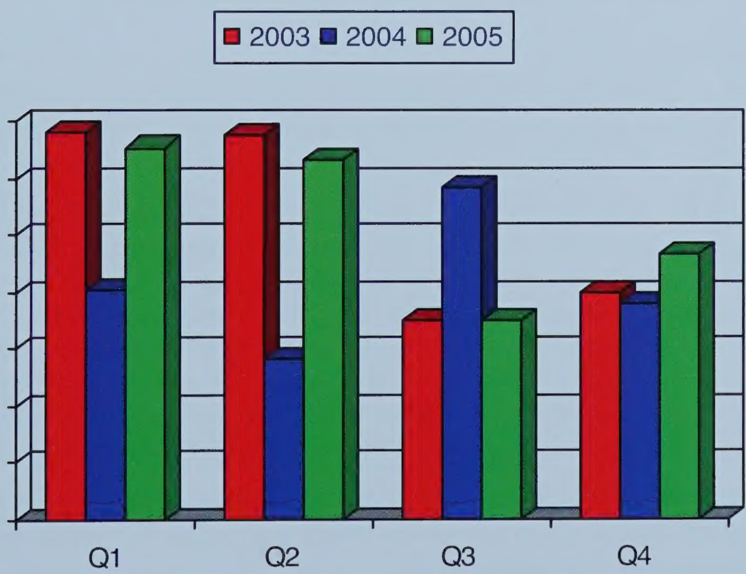
Slave Lake plant - Production Yield



(relative scale)

- Slave Lake average production yield improved by 5% in 2005 when compared to 2004 and by 23% when compared to 2003.

Sundre plant - Production Yield



(relative scale)

- Sundre production yield varied throughout 2005 as the plant has been increasingly used to fill production gaps.

International Operations

Enerchem's international presence has been focused on the oil and gas markets of Egypt and North Africa through its investment in the Egyptian Canadian Company for Chemicals Industries F.Z. ("ECC"). Over the last several years, Enerchem provided its technical expertise to ECC and assisted with the development of a complete line of specialty chemicals to support the manufacturing and laboratory facility situated in the free zone area of Alexandria, Egypt. This facility, being the first Egyptian engineered and constructed specialty chemicals blending facility in Egypt, employs qualified personnel to meet all of the product requirements of its customers.

Health, Safety and Environmental

Enerchem places the importance of safety above all other aspects of the Company's business. Enerchem recognizes that its employees represent its most valuable asset and must be provided with the tools and systems necessary to carry out their work in a safe environment.

We have initiated comprehensive policies and procedures to ensure the health and safety of all our employees, contractors, sub-contractors and visitors.

Enerchem holds a Certificate of Recognition ("COR") for its oilfield operations. The COR recognizes that our health and safety management systems meet the Standards of Partnerships developed by Alberta Human Resources and Employment.

We have also implemented programs and guidelines to eliminate our environmental exposures. All environmental laws and regulations are adhered to, including Alberta's Environmental Protection and Enhancement Act, the Canadian Environmental Protection Act, the Transportation of Dangerous Goods Regulations, and the Environmental Operating Guidelines for the Alberta Petroleum Industry.

Corporate Governance

Full disclosure with respect to the Toronto Stock Exchange Corporate Committee requirements is contained in the Information Circular of Enerchem International Inc., prepared for the Annual General Meeting to be held May 17, 2006.

The main corporate governance practices followed by Enerchem involve the assumption by the directors of responsibility for stewardship of the Company. Enerchem's Board of Directors comprises seven members, six of whom qualify as unrelated directors by virtue of their independence from management or any interest, business or other relationship that could materially interfere with the directors' ability to act in the best interests of the Company. The Board of Directors has four committees being: the Audit Committee, the Compensation Committee, the Environmental Committee and the Strategic Planning and Priorities Committee.

Enerchem is committed to the objectives of the corporate governance policy established by the Toronto Stock Exchange and will continue to work toward complying with the objectives set forth therein.

Management's Discussion and Analysis ("MD&A")

The following MD&A focuses on key statistics from the financial statements and pertains to known risks and uncertainties relating to the oilfield services industry in Western Canada where Enerchem operates. This discussion should not be considered all inclusive, as it excludes changes that may occur in general economic, political and environmental conditions. This discussion and analysis of the financial condition and results of operations for the year ended December 31, 2005 should be read in conjunction with the audited annual financial statements and related notes and material contained in other parts of this Annual Report and the Company's Annual Information Form. Additional information relating to the Company is available on the System for Electronic Document Analysis and Retrieval ("SEDAR") at www.sedar.com. This MD&A was prepared effective March 13, 2006.

Certain statements contained in this Annual Report, including statements contained in this MD&A, that are not historical facts may be considered "forward looking statements." Forward looking statements are often identified by the use of words such as "seek", "anticipate", "plan", "continue", "estimate", "expect", "may", "will", "project", "potential", targeting", "intend", "could", "might", "should", "believe", and similar expressions. Such statements are based on current expectations that involve risks and uncertainties which could cause actual results to differ from those anticipated. Important factors that can cause anticipated outcomes to differ materially from actual outcomes include the impact of general economic conditions, industry conditions, competition from other industry participants, volatility of petroleum prices, the ability to attract and retain qualified personnel, changes in laws or regulations, currency fluctuations, continued ability to access capital from available facilities and environmental risks. The Company believes that the expectations reflected in those forward looking statements are reasonable but no assurances can be given that these expectations will prove to be correct and such forward looking statements included in this Annual Report should not be unduly relied upon. These forward looking statements are made as of the date hereof and the Company assumes no obligation to update or revise them to reflect new events or circumstances. References in this MD&A to "Enerchem", "Company", "us", "we", and "our" mean Enerchem International Inc.

Vision, Core Businesses and Strategy

Enerchem strives to provide its customers with premium products, outstanding service and superior technical expertise in a safe and environmentally conscientious manner, while enhancing value to our shareholders.

Business of the Company

Enerchem International Inc. is a provider of hydrocarbon fluid solutions ("specialty fluids") designed to resolve oilfield processing and production problems. The Company's specialty fluids provide measurable productivity increases, operating and maintenance cost reductions and solutions to environmental problems. The Company's proprietary hydrocarbon products are manufactured through its facilities located in Sundre and Slave Lake, Alberta. The Company's fracturing and drilling fluids and solvents are manufactured at these locations. Enerchem's products are marketed and distributed through its network of sales and service representatives. During the third quarter of 2004, the Company diversified its operations with the establishment of its Energy Marketing group. This diversification was precipitated to maximize value received by the Company for its hydrocarbon by-products, provide energy marketing management and expertise and, to mitigate in part, the Company's exposure to the seasonality of its operations. As a result, the Company's activities are divided into two core business segments: Oilfield Services which represents the manufacture and sale of specialty fluids; and, Energy Marketing which represents the purchasing, gathering and marketing of petroleum for resale to refiners and other customers. The operations of the Company are conducted entirely within the Western Canadian Sedimentary Basin ("WCSB").

The Company's international operations represent a 25% investment in an Egyptian company, Egyptian Canadian Company for Chemicals Industries – F.Z., which operates a blend plant in the free zone area of Alexandria, Egypt. Enerchem has invested $750,000 U.S. in this Egyptian company and accounts for its investment on the cost basis as the Company does not exercise significant influence. As a result, earnings from the Company's Egyptian investment are recognized only to the extent received or receivable.

On December 31, 2005, the Company sold its specialty chemical operations which included inventories and property, plant and equipment for $13,244,000. The net gain on the sale of the specialty chemical operations amounted to $3,747,000 after income taxes of $1,484,000. Details of this divestiture are provided in the notes to the financial statements under note 3, "Discontinued operations". The comparative figures for the year ended December 31, 2004 have been restated for discontinued operations.

Business Strategy

Enerchem's distinct business advantage is that its facilities, situated in Western Canada, are dedicated to providing a diversified range of proprietary hydrocarbon fluids that achieve consistency in product quality to meet

oil and gas processing and production requirements common to the WCSB. The Company wants to capitalize on its position and to provide above average returns on investment to its shareholders. To accomplish this, the Company's business strategy is focused on:

- Becoming a low cost producer of quality hydrocarbon fluids that provide the best customer value;
- Establishing a more consistent revenue base facilitating stable earnings during seasonal slowdowns in oilfield activity; and
- Optimizing infrastructure and facilities capabilities to capture identified market opportunities and provide competitive advantages.

A substantial component of the Company's future organic growth and profitability is incumbent on its continued ability to successfully market and maximize value received for its hydrocarbon fluid products and by-products. This success hinges on the Company's ability to: secure sufficient quantities of crude oil ("feedstock") for its production requirements to meet customer demand; implement cost effective transportation structures; and, its ability to reflect the underlying value of the Company's products to the retail markets. To accomplish this, the Company's business strategy is focused on:

- Securing favourable long-term feedstock arrangements providing opportunity to maximize the Company's production capabilities;
- Optimizing the capabilities of its manufacturing processes and internal know-how;
- Optimizing its fluid transportation arrangements and infrastructure;
- Optimizing its business opportunities and operating synergies available through its energy marketing capabilities.

Key Performance Drivers

Enerchem believes the following key performance drivers are critical to the success of the business:

- Hydrocarbon prices, which influence the capital expenditure programs and resulting oilfield activity levels of exploration and development companies in the WCSB;
- Weather, which affects the Company's ability to operate in key locations of the WCSB;
- Access to, and retention of, qualified personnel;
- Access to hydrocarbon feedstocks compatible with the Company's plant processing and product quality requirements;
- Expectations of its customers respecting oil and gas exploration and development prospects in the WCSB;
- A continued ability to offer competitive product pricing; and
- Continued access to terminalling facilities required by the Energy Marketing segment to accommodate the purchasing, gathering and marketing of petroleum for resale to refiners and other resellers.

There are several key performance measures the Company uses to monitor and assess its performance relative to the key performance drivers, the implementation of its strategy, and the achievement of its goals and vision.

Some of the Company's key financial performance indicators and results against those indicators are set out below:

Key financial performance indicators - continuing operations

For the years ended December 31	2005	2004
Total revenue growth	72%	85%
Revenue growth – Oilfield Services segment	48%	41%
Total gross profit percentage	15%	16%
Gross profit percentage – Oilfield Services segment	17%	18%
Net earnings as a percentage of revenues	3.6%	1.2%
Basic net earnings per common share	$ 0.26	$ 0.05
Return on average capital employed (ROACE)	13.5%	4.4%

Return on average capital employed is calculated as the ratio of earnings before income taxes and interest on debt to average capital assets.

In addition, the Company has key operating performance indicators that include, but are not limited to: market share, product profitability, product quality and assurance, plant productivity, productivity improvements and waste reduction and operating and administrative cost management.

Capability to Deliver Results

Non-Capital Resources

People are the most critical non-capital resource required in order for the Company to achieve its goals set out in its strategic plan. A formal human resource plan has been implemented in order to ensure the Company focuses on improving and maintaining its employee morale. The Company is continually evaluating its human resource levels to determine if levels are adequate and adequately trained to meet its business requirements. The Company believes that it presently has sufficient human resources to successfully operate its business and to execute its strategic plan.

Capital Resources

The Company has the necessary working capital to meet its current obligations and commitments. The Company maintains a fleet of leased field service vehicles and leased premises which represent its off-balance sheet financing arrangements. During 2005, the Company used cash flows from its operating activities and available demand credit facilities with a Canadian bank in order to fund its capital projects in Grande Prairie, Sundre and Slave Lake, Alberta. In order to finance future capital expenditure obligations and future growth, Enerchem anticipates financing its activities through a combination of available cash and cash equivalents, cash flow from operations and utilizing its existing credit facilities. Due to the long term nature of its assets and its historical cost of capital, the Company believes that it must provide an annual return on average capital employed of 10% to 15% over the life of its asset base in order to be financially accretive for shareholders and to minimize Enerchem's cost of capital.

Systems and Processes

The Company's operational systems and processes are continuously reviewed by management. During 2005, the Company completed a review of its compensation system to ensure market competitiveness and to align its human resources to the attainment of the Company's strategic objectives. The Company also continues to evaluate and implement methods and infrastructure to facilitate increased productivity of its fractionation plants in Slave Lake and Sundre and continues to evaluate processes that will contribute to reduce overall feedstock costs. The foregoing systems and process modifications will align the Company to execute its strategic plan.

Controls and Procedures

The Company maintains a set of disclosure controls and procedures designed to ensure that information required to be disclosed in filings made pursuant to Multilateral Instrument 52-109 is recorded, processed, summarized and reported within the time period specified in the Canadian Securities Administrators rules and forms. The Chief Executive Officer and Chief Financial Officer have evaluated the Company's disclosure controls and procedures as of December 31, 2005, and concluded that such disclosure controls and procedures are effective.

Seasonality of Operations

Weather conditions can affect the sale of the Company's products and services. The ability to move heavy equipment in the Canadian oil and natural gas fields is dependent on weather conditions. As a result, spring months in Western Canada and the duration of this "spring breakup" has a direct impact on the Company's activity levels. In addition, many exploration and production areas in the northern WCSB are accessible only in winter months when the ground is frozen hard enough to support the weight of heavy equipment. The timing of freeze up and spring break up affects the ability to move equipment in and out of these areas. As a result, late March through May is traditionally the Company's slowest period.

Trends and Outlook

Industry analysts are expecting that the total wells drilled in the next two years will remain at or near record levels from the number of wells drilled in 2005. Industry analysts are predicting that oil and gas prices will continue to remain at historically high levels. The Company believes that long–term fundamentals require continued exploration and production in the WCSB to meet continued North American and worldwide demand for oil and natural gas and as a result expects strong demand for its products and services in 2006.

Selected Annual Information

Selected annual financial information derived from the audited financial statements for the three most recently completed financial years is set forth below and is prepared in accordance with generally accepted accounting principles in Canada:

For the years ended December 31	2005	2004(1)	2003(2)
	$	$	$
Revenues	109,132,279	63,619,257	34,464,462
Net earnings (loss) from continuing operations	3,884,508	759,654	(814,702)
Net earnings (loss) per share from continuing operations			
Basic	0.26	0.05	(0.06)
Diluted	0.26	0.05	(0.06)
Net earnings (loss) for the year	8,174,738	1,960,700	(525,924)
Net earnings (loss) per share			
Basic	0.55	0.14	(0.04)
Diluted	0.55	0.13	(0.04)
Total assets	73,921,005	61,653,226	52,168,157
Total long-term financial liabilities	1,832,276	3,042,634	1,972,766

(1) Restated to reflect the sale of the Company's specialty chemical operations.

(2) Restated to reflect the sale of the Company's specialty chemical operations and to record stock based compensation expense of $134,787.

Revenues in 2005 increased by 72% when compared to 2004 and were 217% greater than revenues achieved in 2003. The increase in revenues in 2005 when compared to 2004 and 2003 reflects increased activity levels in the WCSB, increased product revenues from our Oilfield Services segment and increased revenues as a result of the Company's diversification into energy marketing during the second half of 2004. On December 31, 2005, the Company sold its specialty chemical operations which included inventories and property, plant and equipment associated with those operations. The net gain on the sale of the discontinued operations amounted to $3,747,000 after income taxes of $1,484,000. Revenues from its discontinued operations were excluded from total revenues in the amount of $15,789,000 for 2005; $17,213,000 for 2004; and, $15,446,000 for 2003. In addition, on December 1, 2003 the Company sold 100% of its wholly owned U.S. subsidiary company, Enerchem International Corporation. As a result, revenues from its discontinued operations were excluded from total revenues in the amount of $1,166,000 for the year ended December 31, 2003.

The improvement in net earnings from continuing operations for fiscal 2005 when compared to fiscal 2004 and 2003 primarily reflects the year-over-year growth in the volume of products sold which was largely influenced by the effects of increased activity levels in the WCSB and continued improvements in the Company's fractionation plant manufacturing capabilities. During 2005, the Company continued to achieve improved productivity from its Slave Lake plant which resulted in improved production yields and plant utilization when compared to the plant's productivity rates in 2004 and its first year of operation in 2003. The improvement in net earnings was also achieved through the operations of the Company's Energy Marketing segment which provided improved pricing arrangements for its by-products.

The Company's total assets have increased steadily since 2003. The increase in total assets in 2005 when compared to 2004 and 2003 reflects the growth experienced by the Company's Oilfield Services segment combined with the added growth in operations provided by the Company's Energy Marketing segment. The Company's long-term liabilities decreased in 2005 when compared to 2004, as the Company utilized its cash flow from operations and an available demand credit facility with a Canadian chartered bank to finance major capital expenditures undertaken in 2005.

Discontinued Operations

On December 31, 2005, the Company sold its specialty chemical operations which included inventories and property, plant and equipment associated with those operations. The net gain on the sale of the discontinued operations amounted to $3,747,000 after income taxes of $1,484,000. Revenues from its discontinued operations were excluded from total revenues in the amount of $15,789,000 for 2005 and $17,213,000 for 2004. Details of the divestiture are provided in the notes to the audited financial statements under note 3, "Discontinued Operations".

Results of Continuing Operations - Annual

Total Revenues

For the years ended December 31	2005		2004		Change
	$	%	$	%	%
Oilfield Services	72,072,308	66	48,667,303	76	48
Energy Marketing	37,059,971	34	14,951,954	24	148
Total	109,132,279	100	63,619,257	100	72

The Company's total revenues increased by 72% in 2005 when compared to 2004. The increase in revenues was largely influenced by: high levels of oilfield activity and demand for the Company's fluids in the principal regions serviced by the Company; the overall increase in commodity prices which precipitated increased retail pricing of the Company's products; and, contributions from the Energy Marketing segment which generated a full year of revenues in 2005 when compared to 2004 as this business segment was initiated at the commencement of the third quarter of 2004.

Segmented Revenues

Oilfield Services

The Company's Oilfield Services segment is focused on manufacturing and selling specialty fluids which are comprised of three product categories: fracturing, drilling and solvent fluids. Oilfield Services' products are designed to provide measurable productivity increases, operating and maintenance cost reductions and solutions to environmental problems. The Oilfield Services' manufacturing facilities are situated in Sundre and Slave Lake, Alberta and are dedicated to providing proprietary specialty fluids and supporting services designed to ensure consistency in product quality to meet oil and gas processing and production requirements common to the WCSB.

Product Revenues -Oilfield Services

For the years ended December 31	2005	2004	Change
	$	$	%
Fracturing	32,954,141	31,542,280	5
Drilling	22,482,392	5,186,919	333
Solvents	9,732,722	6,553,170	49
By-products - other	6,903,053	5,384,934	28
Total	72,072,308	48,667,303	48

Revenues from the Oilfield Services segment increased by 48% in 2005 when compared to the same period last year. During 2005, the Company experienced unprecedented demand for its drilling fluids largely as a result of the continuation of high levels of oilfield activity in the principal regions serviced by the Company and on-going initiatives undertaken by the Company focused on increasing its share of the drilling fluids market. As a result, the Company achieved record drilling fluid revenues in 2005 of $22,482,000 which represented an increase of 333% when compared to last year. While fracturing fluid revenues reached all time record levels in 2005, the increase was largely price related which was influenced by the underlying increased cost of feedstock in 2005. During the first quarter of 2005 the Company experienced a shortfall in available crude oil and the crude's quality not meeting specifications of the Slave Lake facility which created an inability for the Company to meet the increased demand for both fracturing and drilling fluids. As a result, during the first quarter of 2005, the Company's increase in drilling fluid revenues and volumes was at the expense of a reduction in the volume of fracturing fluid sold. The improvement in solvent revenues in 2005 when compared to 2004 resulted from the Company's re-focus and success in marketing its products in specific regions of northern and central Alberta.

Energy Marketing

During the third quarter of 2004, the Company diversified its operations with the establishment of its Energy Marketing group. This diversification was precipitated to maximize value received by the Company for its hydrocarbon by-products, provide energy marketing management and expertise and, to mitigate in part, the Company's exposure to the seasonality of its operations. Energy Marketing represents the purchasing, gathering and marketing of petroleum for resale to refiners and other resellers. During the second quarter of 2005, the third party owned facility used by the Company in conducting its energy marketing activities was affected by a change of ownership which limited the operational flexibility previously available to the Energy Marketing segment. The Company continues to pursue opportunities that will complement its energy marketing activities.

Revenues from the Energy Marketing segment increased by 148% in 2005 when compared to 2004 as the segment generated a full year of revenues in 2005 when compared to 2004 as this business segment was initiated at the commencement of the third quarter of 2004.

Gross Profit

For the years ended December 31	2005	2004	Change
	$	$	%
Total Gross Profit	16,674,725	10,212,509	63
% of Total Revenues	15%	16%	
Oilfield Services	12,494,996	8,888,376	41
% of Oilfield Services revenues	17%	18%	
Energy Marketing	4,179,729	1,324,133	216
% of Energy Marketing revenues	11%	9%	

Total Gross Profit increased by 63% in 2005 when compared to 2004 as a result of the year-over-year growth in the volume of products and by-products sold. While total gross profit as a percent of total revenues declined to 15% in 2005 from 16% in 2004, this reduction was largely influenced by the margin compression experienced from the sale of by-products not marketable by the Company's Energy Marketing segment during 2005. Conversely, the Company's product margins for specialty fluids in 2005 were consistent with product margins achieved in 2004. The stability of specialty fluid margins were maintained on a comparative year basis, notwithstanding the 31% increase in feedstock costs and overall increase in third party transportation costs in 2005.

Energy Marketing gross profit increased by 216% in 2005 when compared to 2004 due to the contribution of a full year of operating activity from this segment in 2005 which commenced its operations during the third quarter of 2004. The improvement in the Energy Marketing gross profit as a percent of the segment's revenues in 2005 when compared to 2004 resulted from opportunities to optimize crude oil heavy and light stream differentials.

Operating Expenses

Salaries and employee benefits

For the years ended December 31	2005	2004	Change
	$	$	%
Expense amount	4,892,698	4,237,582	15
% of gross profit margin	29%	41%	

The 15% increase in salary costs in 2005 when compared to 2004 resulted from the increase in sales and energy marketing staff compensation costs precipitated by higher activity levels and the increase in plant compensation costs as a result of higher staffing levels.

Selling, general and administration

For the years ended December 31	2005	2004	Change
	$	$	%
Expense amount	4,864,165	3,342,957	46
% of gross profit margin	29%	33%	

Selling, general and administration (SG&A) costs increased by 46% in 2005 when compared to 2004 as a result

of general plant repairs and maintenance and plant turnaround costs associated with the Company's fractionation plants. Effective April 1, 2005, the Company implemented a scheduled turnaround maintenance program for its fractionation plants which requires the shutdown of its facilities for significant overhaul and refurbishment. For the year ended December 31, 2005, $342,000 of turnaround costs were amortized and included in SG&A expense. Fiscal 2005 also reflects a full year of costs associated with the Company's increase in its fleet of trailers used for hauling fluids. The additional trailers were acquired during the fourth quarter of 2004. In addition, SG&A expense reflects higher fuel and operating costs associated with the Company's fleet of service and delivery vehicles precipitated by increased oilfield activity levels.

Depreciation and amortization

For the years ended December 31	2005	2004	Change
	$	$	%
Depreciation	680,349	1,134,635	(40)
Amortization	8,675	6,229	39
Total amount	689,024	1,140,864	(40)
% of gross profit margin	4%	11%	

Depreciation and amortization expense decreased by 40% in 2005 when compared to 2004. Effective January 1, 2005, the Company changed its estimated useful lives of the fractionation processing facilities and began to depreciate its fractionation facilities on a straight-line basis, which incorporates the change in the plants expected useful lives which range from 29 to 37 years. The Company has also established estimated salvage values for these facilities based on accepted industry standards. A salvage value of $750,000 has been established for the Slave Lake facility and $250,000 has been established for the Sundre facility. Prior to January 1, 2005, the Company depreciated its fractionation plants on a declining balance basis at annual rates ranging from 5% to 10%. The impact of this change relative to the previous method of depreciation was a reduction in depreciation expense for the year ended December 31, 2005 of $473,000.

Income Taxes

For the years ended December 31	2005	2004	Change
	$	$	%
Expense amount	2,052,996	526,855	290
Effective tax rate	35%	41%	

The provision for income taxes in 2005 includes current taxes payable of $1,128,000 compared to $nil in 2004 as a result of the increased taxable income in 2005. At December 31, 2004 the Company had non-capital losses available for carry forward of $1,478,000 which were applied to reduce 2005 taxes payable.

The reduction in the effective tax rate in 2005 to 35% from 41% in 2004 resulted from the decline in non-deductible expenditures for income tax purposes.

Net Earnings

For the years ended December 31	2005	2004	Change
	$	$	%
Continuing operations	3,884,508	759,654	411
Earnings per share, diluted	0.26	0.05	420
EBITDA, continuing operations (1)	6,974,289	2,775,881	151
Discontinued operations	4,290,230	1,201,046	257
Earnings per share, diluted	0.29	0.08	263
Net earnings for the year	8,174,738	1,960,700	317
Earnings per share, diluted	0.55	0.13	323

(1) EBITDA is a non-GAAP measure which the Company defines as earnings before interest , taxes, depreciation, amortization and accretion expense.

Net earnings from continuing operations for the year ended December 31, 2005 reflects a 411% increase over the previous year as a result of the year-over-year growth in the volume of products sold, which was largely influenced by the effects of increased activity levels in the WCSB and continued improvements in the Company's fractionation plant manufacturing capabilities. During 2005, the Company continued to achieve improved productivity from its Slave Lake plant, which resulted in improved production yields and plant utilization when compared to the plant's productivity rates in 2004. In addition, the improvement in net earnings was also achieved through the operations of the Company's Energy Marketing segment which provided improved pricing arrangements for its by-products.

The Company's EBITDA from continuing operations increased by 151% in 2005 when compared to the previous year as a result of the significant improvement in activity levels.

Summary of Quarterly Results

The following tables provide selected unaudited financial information relating to the Company's quarterly activities in 2005 and 2004 and are prepared in accordance with Canadian generally accepted accounting principles with respect to the preparation of interim financial statements.

2005 (1)
Three month period ended
(unaudited)

	December 31	September 30	June 30	March 31
	$	$	$	$
Revenues	31,380,017	27,896,098	19,910,693	29,945,471
Net earnings from continuing operations	1,701,475	699,772	425,952	1,057,309
Net earnings per share from continuing operations				
Basic	0.11	0.05	0.03	0.07
Diluted	0.11	0.05	0.03	0.07
Net earnings for the period	5,586,835	850,722	336,239	1,400,942
Net earnings per share for the period				
Basic	0.37	0.06	0.02	0.10
Diluted	0.37	0.06	0.02	0.10

(1) The information for the first three quarters of 2005 have been restated for discontinued operations.

2004 (2)
Three month period ended
(unaudited)

	December 31	September 30	June 30	March 31
	$	$	$	$
Revenues	26,340,467	18,487,842	4,915,178	13,875,770
Net earnings (loss) from continuing operations	137,982	339,138	(315,930)	598,464
Net earnings (loss) per share from continuing operations				
Basic	0.01	0.02	(0.02)	0.04
Diluted	0.01	0.02	(0.02)	0.04
Net earnings (loss) for the period	396,405	606,669	(53,987)	1,011,613
Net earnings (loss) per share for the period				
Basic	0.03	0.04	-	0.07
Diluted	0.03	0.03	-	0.07

(2) The information for the quarters during the 2004 year have been restated for discontinued operations.

On a quarter to quarter basis, revenues and earnings from continuing operations in 2005 increased in all four quarters when compared to 2004. This reflects increased activity levels in the WCSB, increased product revenues and earnings from the Oilfield Services segment and increased revenues as a result of the Company's diversification into energy marketing in 2004. On December 31, 2005, the Company sold its specialty chemical operations which included the inventories and property, plant and equipment associated with those operations. The net gain on the sale of the discontinued operations amounted to $3,747,000 after income taxes of $1,484,000. The trend in quarter to quarter revenues also reflects the seasonality of operations. The Company traditionally experiences increased activity levels during the fall and winter seasons and decreased activity during periods affected by wet or unseasonable weather conditions. Enerchem's hydrocarbon fracturing and drilling fluids are primarily used for deep well drilling and applications common to the foothills region and northern Alberta and British Columbia, areas known for deeper drilling. Oil and gas activity in these geographic regions is normally strong during winter months or when climatic conditions are favourable.

Liquidity and Capital Resources

Cash provided from continuing operations before non-cash working capital items for 2005 was $5,948,000 compared to $2,765,000 in 2004. The increase in cash flows was largely driven by the improvement in net earnings in 2005. As at December 31, 2005 the Company had positive working capital of $23,554,000 compared to $11,433,000 at December 31, 2004. Cash proceeds received from the sale of the Company's discontinued operations on December 31, 2005 and the increase in sales activity levels largely contributed to the improvement in the Company's working capital position. The Company's current ratio (defined as current assets divided by current liabilities) was 2.19 to 1 at December 31, 2005 compared to 1.67 to 1 at December 31, 2004. The Company has a bank operating line of credit in the amount of $15,000,000, subject to margining requirements, to finance its working capital requirements. At December 31, 2005, $3,228,000 was drawn by the Company from its available operating line of credit. The Company has a $5,000,000 bank guarantee facility available as security for its feedstock arrangements and purchase commitments. At December 31, 2005 the Company did not have any outstanding bank guarantees.. As at the date of this MD&A, the Company is in compliance with all debt covenants and obligations. The terms of the credit facility with the bank provide that non-revolving loans, while repayable on demand by the bank, will not be demanded by the bank unless the Company is in default of its obligations and covenants and if, in the opinion of the bank, there has been a change in the business, financial condition, operations or conduct of the Company. The Company believes that it has sufficient liquidity to operate its business and to execute its strategic plan.

Net cash provided by investing activities from continuing operations were $6,583,000 in 2005 compared to net cash used of $2,381,000 in 2004. Investing activities for the year included proceeds of $10,204,000 from the sale of property, plant and equipment related to the discontinued operations. Proceeds received from the sale, after repayment of bankers acceptances, were deposited in short-term interest bearing securities. Cash used for investing activities of $3,691,000 in 2005 (2004 - $2,710,000) were directed to facilities improvement and expansion projects in Grande Prairie, Sundre and Slave Lake, Alberta. Capital expenditures during the current year and prior year were funded from operating cash flows and the Company's available credit facilities.

Net cash used in financing activities from continuing operations were $909,000 in 2005 compared to net cash provided by financing activities from continuing operations of $1,178,000 in 2004. Proceeds from the issuance of common shares through the Company's employee share purchase plan and upon exercise of stock options were $508,000 in 2005 compared to $697,000 in 2004. During 2005, the Company made long-term debt repayments of $1,168,000 reducing its long-term debt outstanding to $3,048,000 at December 31, 2005 from $4,216,000 at December 31, 2004. Subsequent to December 31, 2005, the Company repaid its long-term debt outstanding of $3,048,000.

Summary of Contractual Obligations and Off-Balance Sheet Arrangements

The following table summarizes the Company's contractual obligations including payments due for each of the next five years and thereafter.

Contractual obligations (in Canadian dollars)	Total	Payments due by period Less than 1 year	1 – 3 years	4 – 5 years	After 5 years
	$	$	$	$	$
Long term debt (1)	3,047,764	1,215,488	725,201	375,894	731,181
Operating leases (2)	793,096	427,002	251,615	114,479	-
Total contractual obligations	3,840,860	1,642,490	976,816	490,373	731,181

(1) Represents non-revolving bank loans provided through a credit facility with a Canadian chartered bank and are repayable in blended monthly payments of $113,526 and mature at varying dates from May 2006 to May 2020.
(2) Represents normal operating leases comprised of vehicles, trailers and office space.

In the normal course of business with vendors, the Company may become contingently liable for performance under letters of guarantee and credit. In this regard, the Company has arranged a $5,000,000 bank guarantee facility available as security for its feedstock arrangements and purchase commitments. At December 31, 2005 the Company did not have any outstanding bank guarantees and letters of credit.

Subsequent to December 31, 2005, the Company repaid the demand non-revolving loans in the amount of $3,047,764.

For 2006 the Company expects cash flow from operations and from its sources of financing to be sufficient to meet its contractual obligations and off-balance sheet arrangements.

Share Capital

As at December 31, 2005 the Company had 14,820,807 common shares outstanding. In addition, as at that date the Company has reserved 1,026,000 common shares for issuance under outstanding stock options.

Results of Continuing Operations - Fourth Quarter

The following unaudited interim financial statements reflect the results of operations for the three months ended December 31, 2005 and 2004.

Three months ended December 31	2005	2004(1)
	$	$
Revenues	31,380,017	26,340,467
Cost of sales	25,611,786	23,307,396
Gross profit	5,768,231	3,033,071
Expenses		
Salaries and employee benefits	1,131,669	1,213,145
Selling, general and administration	1,731,309	990,631
Depreciation and amortization	201,873	326,069
Accretion expense	1,100	32,059
Amortization of pre-operating costs	21,718	21,718
Interest expense	55,738	62,469
	3,143,407	2,646,091
Earnings from continuing operations before other expense	2,624,824	386,980
Other expense	9,520	83,940
Earnings from continuing operations before income taxes	2,615,304	303,040
Income taxes	913,829	165,058
Net earnings from continuing operations	1,701,475	137,982
Net earnings from discontinued operations	3,885,360	258,423
Net earnings for the period	5,586,835	396,405

(1) restated to reflect discontinued operations

Total Revenues

Three months ended December 31	2005		2004		Change
	$	%	$	%	%
Oilfield Services	21,050,928	67	18,383,953	70	15
Energy Marketing	10,329,089	33	7,956,514	30	30
Total	31,380,017	100	26,340,467	100	19

The Company's total revenues increased by 19% during the fourth quarter of 2005 when compared to the same period of 2004, which reflects the continued strength in oilfield activity, growth in demand for the Company's specialty fluids and product price increases as a result of higher commodity prices.

Segmented Revenues

Oilfield Services

Three months ended December 31	2005	2004	Change
	$	$	%
Fracturing	10,267,064	10,061,901	2
Drilling	8,050,516	2,982,086	170
Solvents	2,733,348	1,684,050	62
By-products – other	-	3,655,916	(100)
Total	21,050,928	18,383,953	15

Revenues from the Oilfield Services segment increased by 15% for the fourth quarter of 2005 when compared to the same period last year. The overall increase in drilling fluid and solvent revenues was attributable to both volume and price increases as a result of high levels of activity in the principal regions serviced by the Company. While fracturing fluid revenues increased moderately on a comparative quarter basis, the increase in revenues reflects price increases due to the underlying increase in feedstock costs. On a comparative quarter basis, the

volume of fracturing fluid sold by the Company has declined as a direct result of the effects of higher commodity prices on oil based frac fluids. The higher pricing environment for oil based fracs has recently caused more end-users to turn to water based fracturing fluids as an alternative fluid. The Company is investigating opportunities to be more competitive with water based fracs. The completion of the Company's feedstock tank farm in Slave Lake during the third quarter of 2005 precipitated the termination of a previous arrangement with a third party crude oil marketer, which secured by-products from the Slave Lake facility for their operations. The termination of this arrangement allowed the Company to optimize values received for by-products produced from its Slave Lake plant through its Energy Marketing segment.

Energy Marketing

Revenues from the Energy Marketing segment increased by 30% on a comparative quarter basis due to the increase in by-product volumes managed by this segment. During the fourth quarter of 2005, all of the Company's by-products produced at the Sundre and Slave Lake plants were available for the segments blending operations.

Gross Profit

Three months ended December 31	2005	2004	Change
	$	$	%
Total Gross Profit	5,768,231	3,033,071	90
% of Total Revenues	18%	12%	
Oilfield Services	4,329,469	2,377,843	82
% of Oilfield Services revenues	21%	13%	
Energy Marketing	1,438,762	655,228	120
% of Energy Marketing revenues	14%	8%	

Total Gross Profit increased by 90% for the fourth quarter of 2005 when compared to the same period in 2004 as a result of the year-over-year growth in the volume of products and by-products sold combined with initiatives undertaken by the Company to optimize its transportation of product deliveries and to offset underlying increases in feedstock costs by modifying its retail product prices. As a result of these initiatives, Oilfield Services gross profit as a percent of Oilfield Services revenues for the fourth quarter of 2005 improved to 21% compared to 13% for the same period last year.

Energy Marketing gross profit increased by 120% during the fourth quarter of 2005 when compared to the same period last year as a direct result of the increase in by-product volumes managed by this segment. The completion of the Company's feedstock tank farm in Slave Lake during the third quarter of 2005 precipitated the termination of a previous arrangement with a third party crude oil marketer which secured by-products from the Slave Lake facility for their operations. The termination of this arrangement allowed the Company to optimize values received for by-products produced from its Slave Lake plant. For the fourth quarter of 2005, the improvement in the Energy Marketing gross profit as a percent of the segment's revenues when compared to the same period last year resulted from opportunities to optimize crude oil heavy and light stream differentials.

Operating Expenses

Salaries and employee benefits

Three months ended December 31	2005	2004	Change
	$	$	%
Expense amount	1,131,669	1,213,145	(7)
% of gross profit margin	20%	40%	

The 7% decrease in salary costs on a comparative quarter basis resulted from the reorganization of certain business units within the Company and non-replacement of staff comprising these units.

Selling, general and administration

Three months ended December 31	2005	2004	Change
	$	$	%
Expense amount	1,731,309	990,631	75
% of gross profit margin	30%	33%	

SG&A costs increased by 75% for the quarter ended December 31, 2005 when compared to the same period in 2004 as a result of general plant repairs and maintenance and plant turnaround costs associated with the Company's fractionation plants. In addition, SG&A expense reflects higher fuel and operating costs associated with the Company's fleet of service and delivery vehicles precipitated by increased oilfield activity levels.

Depreciation and amortization

Three months ended December 31	2005	2004	Change
	$	$	%
Depreciation	199,704	323,900	(38)
Amortization	2,169	2,169	-
Total amount	201,873	326,069	(38)
% of gross profit margin	3%	11%	

Depreciation and amortization expense decreased by 38% for the quarter ended December 31, 2005 when compared to the same period last year. Effective January 1, 2005, the Company changed its estimated useful lives of the fractionation processing facilities. Prior to January 1, 2005, the Company depreciated its fractionation plants on a declining balance basis at annual rates ranging from 5% to 10%. Effective January 1, 2005, the Company began to depreciate its fractionation facilities on a straight-line basis which incorporates the change in the plants expected useful lives, which range from 29 to 37 years. The impact of this change relative to the previous method of depreciation was a reduction in depreciation expense for the three months ended December 31, 2005 of $131,000.

Net Earnings

Three months ended December 31	2005	2004	Change
	$	$	%
Continuing operations	1,701,475	137,982	1,133
Earnings per share, diluted	0.11	0.01	1,000
EBITDA, continuing operations (1)	2,895,733	745,355	288
Discontinued operations	3,885,360	258,423	1,403
Earnings per share, diluted	0.26	0.02	1,200
Net earnings for the period	5,586,835	396,405	1,309
Earnings per share, diluted	0.37	0.03	1,133

(1) EBITDA is a non-GAAP measure which the Company defines as earnings before interest , taxes, depreciation, amortization and accretion expense

Net earnings from continuing operations for the three months ended December 31, 2005 reflects a 1,133% increase over net earnings for the comparative quarter last year. The improvement in earnings reflects the quarter-over-quarter growth in the volume of products sold, which was largely influenced by the effects of increased activity levels in the WCSB and continued improvements in the Company's fractionation plant manufacturing capabilities. In addition, the improvement in net earnings was also achieved through the operations of the Company's Energy Marketing segment, which provided improved pricing arrangements for its by-products.

The Company's EBITDA from continuing operations increased by 288% for the fourth quarter of 2005 when compared to the previous quarter last year as a result of the significant improvement in activity levels and earnings performance.

Critical Accounting Policies

The Company's financial statements have been prepared in accordance with Canadian generally accepted accounting principles and include estimates that reflect management's estimates and assumptions that affect the reported amounts of assets and liabilities, the disclosure of contingent assets and liabilities at the date of the financial statements and revenue and expenses for the period reported. Estimates are based upon historical experience and various other assumptions that reflect management's best judgments. These estimates are evaluated periodically and form the basis for making judgments regarding the carrying values of assets and liabilities and the reported amount of revenue and expenses. Actual results could differ from these estimates. The following discussion outlines the accounting policies and practices and management's estimates that are critical to determining Enerchem's financial results.

Goodwill Impairment

The Company tests goodwill for impairment annually and whenever events or circumstances make it more likely than not that an impairment may have occurred, such as a significant adverse change in the business climate or a decision to sell or dispose of a reporting unit. Determining whether impairment has occurred requires valuation

of the respective reporting unit, which is estimated using discounted cash flow methodology. When available and as appropriate, comparative market multiples are used to corroborate discounted cash flow results. In applying this methodology, a number of factors are relied upon, including actual operating results, future business plans, economic projections and market data. During the year, management performed its annual evaluation of the carrying value of goodwill and concluded that goodwill of its reporting units was not impaired.

Property, Plant and Equipment

Property, plant and equipment ("PP&E") are recorded at cost and are depreciated over their estimated useful lives on a declining balance basis, except for the fractionation processing facilities which are depreciated on a straight-line basis. Judgment is involved in determining the useful life of the PP&E and the appropriate annual depreciation rate. The Company's investment in PP&E results in depreciation expense being a significant component of operating expenses of the Company and any misjudgment in determining the useful life and annual depreciation rate could result in a misstatement of depreciation expense.

Income Taxes

The provision for income taxes is calculated based on the expected tax treatment of transactions recorded in the Company's financial statements. Income tax assets and liabilities, both current and future, are measured according to the income tax legislation that is expected to apply when the asset is realized or when the liability settled. If the Company's interpretations differ from those of tax authorities or judgments with respect to tax losses change, the income tax provision could increase or decrease, potentially significantly, in future periods.

Changes in Accounting Policies and Practices

Impairment of Long-Lived Assets

The Company prospectively adopted the CICA recommendations in respect of the impairment of long-lived assets. A long-lived asset is an asset that does not meet the definition of a current asset. This standard requires recognition of an impairment loss when the carrying value of a long-lived asset is not recoverable and exceeds its fair value. Under the standard, an impairment loss is measured as the amount by which the carrying value of the long-lived asset exceeds its fair value. During the year, management assessed the carrying value of the Company's long-lived assets and concluded that the carrying value of its long-lived assets were not impaired.

Asset Retirement Obligations

The Company adopted the CICA recommendations relating to asset retirement obligations, which includes site restoration costs. This standard requires that obligations associated with the retirement of tangible long-lived assets and associated retirement costs be recognized in the period incurred if a reasonable estimate of fair value can be made. The present value of the estimated asset retirement cost is added to the carrying amount of the related long-lived asset. The depreciation of the capitalized asset retirement cost will be determined on a basis consistent with depreciation of the applicable asset. The asset retirement obligation liability is increased at the end of each period to reflect the passage of time and changes in the estimated future cash flows underlying the initial fair value measurement. Upon adoption of this standard, the Company recorded $137,000 as the current fair value of its expected cost as its initial asset retirement obligation ("ARO"). In accordance with the recommendations of this Section, the Company has recorded an accretion expense of $11,000 (December 31, 2004 - $32,000) in the current year. During the year, management assessed the fair value measurement of its initial ARO and concluded that no changes were required.

Hedging Relationships

The CICA issued Accounting Guideline 13 ("AcG 13"), "Hedging Relationships", to clarify circumstances in which hedge accounting is appropriate. The guideline requires that all financial instruments that do not qualify as a hedge under the AcG 13, or are not designated as a hedge, be recorded in the balance sheet as either an asset or a liability with changes in fair value recognized in earnings. The Company enters into numerous financial instruments to manage its commodity price risk that do not qualify as hedges under the new accounting guideline. As a result, the Company has elected to not apply hedge accounting to any of its financial instruments.

Consolidation of Variable Interest Entities

The CICA has issued Accounting Guideline 15, Consolidation of Variable Interest Entities. A Variable Interest Entity ("VIE") is an entity that lacks sufficient appropriate equity to finance its activities or whose equity holders lack adequate decision-making ability. Almost any legal structure used to hold assets or conduct activities might be a variable interest entity, including corporations, partnerships, limited liability companies, majority-owned subsidiaries and trusts.

Under the standard, an entity must consolidate a VIE if it holds equity investments, guarantees, subordinated loans, derivatives or other "variable interests" in the VIE that expose the entity to the majority of the VIE's "expected losses". If no one entity has exposure to the majority of expected losses of the VIE, the entity with the majority of its "expected residual returns" must consolidate it.

This new Guideline became effective for annual and interim periods beginning on or after November 1, 2004. The adoption of this guideline had no impact on the Company's financial results.

Turnaround Maintenance Costs

Effective April 1, 2005, the Company implemented a scheduled turnaround maintenance program for its fractionation plants which requires the shutdown of its facilities for significant overhaul and refurbishment. The Company expects to execute its scheduled turnaround program during the second quarter of each year. Costs of major fractionation plant maintenance are charged to operations over a one year period. At December 31, 2005 unamortized turnaround costs in the amount of $173,520 are included in other assets. For the year ended December 31, 2005, $342,172 of turnaround costs were amortized and included in selling, general and administration expense. Normal repairs and maintenance to the fractionation plants are expensed as incurred.

Property, Plant and Equipment

Effective January 1, 2005, the Company changed its estimated useful life of the fractionation processing facilities and began to depreciate its fractionation facilities on a straight-line basis which incorporates the change in the plants' expected useful lives which range from 29 to 37 years. The Company has also established estimated salvage values for these facilities based on accepted industry standards. A salvage value of $750,000 has been established for the Slave Lake facility and $250,000 has been established for the Sundre facility. Prior to January 1, 2005, the Company depreciated its fractionation plants on a declining balance basis at annual rates ranging from 5% to 10%. The impact of this change relative to the previous method of depreciation was a reduction in depreciation expense for the year ended December 31, 2005 of $473,172.

Financial Instruments and Other Instruments

Fair Values

The carrying values of cash, accounts receivable, promissory note, accounts payable and accrued liabilities and bank indebtedness approximate their fair value due to the relatively short periods at maturity on these instruments. The fair value of the Company's long term debt is estimated based on market prices for same or similar instruments and approximates carrying value.

Credit Risk

The Company's Oilfield Services segment does not have a significant exposure to any individual customer or other party. The Company's Energy Marketing revenues are attributable to several large oil & gas producers and oilfield services companies which account for all of this segment's revenues. Concentration of credit risk on the Company's trade accounts receivable exists in the oil and gas industry. Management believes that the Company is exposed to minimal credit risk since the majority of its business is conducted with major companies in the industry.

Petroleum Prices

The Company is exposed to changes in petroleum and natural gas prices as a result of its use of petroleum feedstock and natural gas for processing at its Sundre and Slave Lake fractionation plants. The potential fluctuations in petroleum and natural gas prices could have a significant impact on the cost of producing its products and the profitability of the Company. To mitigate the affects on profitability of upward changes in petroleum prices, the Company implements product price increases to reflect their underlying values. This ability, however, is sensitive to competitive product pressures. In addition, this risk is reduced in part, from time to time, through the use of crude oil and natural gas forward purchase contracts. The contracts are not used for speculative trading purposes. Realized gains or losses on these contracts are reported as adjustments to petroleum and natural gas costs in the related production period.

As at December 31, 2005 the Company did not have any outstanding crude oil and natural gas forward purchase contracts.

Interest Rate Risk

The Company manages its interest rate risk on borrowings by utilizing a combination of short term fixed rates through the use of 30 to 90 day Banker's Acceptance rates and floating rates on debt. At December 31, 2005 bank indebtedness represented the Company's use of its available demand operating line of credit.

Health, Safety and Environmental

The Company has achieved and maintained a Certificate of Recognition, which is given to employers who develop health and safety programs to meet standards established by the Petroleum Industry Training Service and Alberta Human Resources and Employment. The Company has safety and environmental personnel responsible for maintaining and developing the Company's policies and monitoring the Company's operations to ensure compliance with established policies. However, there can be no assurances that the Company's

procedures will prevent environmental damage occurring from spills of materials handled by the Company. The safety and environmental personnel report directly to the President and Chief Executive Officer of the Company.

Competition and Industry Conditions

The capital expenditure programs of oil and gas companies largely affect the services provided by the Company. The magnitude of capital expenditures determines the demand for the Company's services in providing hydrocarbon fluid solutions to the oil and gas production industry. The primary catalysts to high expenditures and activity levels in the energy industry are oil and gas prices which, in turn, are influenced strongly by supply and demand expectations. The ability to forecast the price of crude oil or natural gas is extremely difficult as many global factors affecting commodity prices are beyond the control of the Company.

There is a strong correlation between drilling activity and demand for the Company's hydrocarbon fracturing and drilling fluids. Industry demand for the Company's fracturing and drilling products is further determined by activity levels that are focused on deep well drilling and applications common to the foothills region and northern Alberta and British Columbia, areas known for deeper drilling. Oil and gas activity in these geographic regions is normally strong during winter months or other times when climatic conditions are favourable. In addition, as our specialty fluids and services are sold in highly competitive markets, the Company's revenues and earnings can be affected by changes in competitive prices and new technologies and methods.

Operating Risk and Insurance

Enerchem has an insurance and risk management program in place to protect its assets, operations and employees. The Company's operations are, however, subject to risks inherent in the oil and gas industry such as malfunction and failures and natural disasters with resultant fluid spills, explosions and fires. These risks could expose the Company to substantial liability for personal injury, loss of life, business interruption, property damage or destruction, pollution and other environmental damages. Although the Company has obtained insurance against certain risks to which it is exposed, such insurance is subject to coverage limits and no assurance can be given that such insurance will be adequate to cover the Company's liabilities or will be generally available in the future or, if available, that premiums will be commercially justifiable. If the Company were to incur substantial liability and such damages were not covered by insurance or were in excess of policy limits, its business, results of operations and financial condition could be materially adversely affected.

Subsequent Event

Proposed Transaction

On March 13, 2006, Enerchem announced that it had signed a Letter of Intent to purchase all of the issued and outstanding shares of Millard Trucking Ltd. and J.D.M. Trucking Ltd., for an undisclosed cash amount. Millard Trucking Ltd. and J.D.M. Trucking Ltd., are related companies headquartered in Sundre, Alberta. The companies' services have been focused on the transportation of fluids and other related oilfield services in central and southern Alberta. The companies maintain a fleet of tank trucks, trailers, vacuum trucks, steamers and pressure trucks and presently employ 29 employees, which includes 22 full time drivers.

The transaction is anticipated to close on or before April 30, 2006, subject to satisfactory completion of the Company's due diligence, approvals from its Board of Directors and the Toronto Stock Exchange.

Management's Responsibility

The management of Enerchem International Inc. is responsible for the preparation of the accompanying financial statements and the preparation of all information in the annual report. The financial statements have been prepared in accordance with accounting principles generally accepted in Canada and are considered by management to present fairly the financial position and operating results of the Company.

The Company maintains various systems of internal control to provide reasonable assurance that transactions are appropriately authorized and recorded, that assets are safeguarded and that financial records are properly maintained to provide accurate and reliable financial statements.

The Board of Directors of the Company carries out its responsibility for the financial statements through its Audit Committee. The Audit Committee has and will meet periodically with the Company's management and independent auditors to review financial reporting matters and internal controls and to review the financial statements. The Audit Committee reported its findings to the Board of Directors who have approved the financial statements.

The Company's independent auditors, PricewaterhouseCoopers LLP, Chartered Accountants, have examined the financial statements whose findings are contained in this annual report.

Douglas F. Robinson
President & Chief Executive Officer

Brian M. Zubach, CMA
Chief Financial Officer

Auditors' Report

To the Shareholders of
Enerchem International Inc.

We have audited the balance sheets of Enerchem International Inc. as at December 31, 2005 and 2004 and the statements of operations and retained earnings and cash flows for the years then ended. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with Canadian generally accepted auditing standards. Those standards require that we plan and perform an audit to obtain reasonable assurance whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation.

In our opinion, these financial statements present fairly, in all material respects, the financial position of the Company as at December 31, 2005 and 2004 and the results of its operations and its cash flows for the years then ended in accordance with Canadian generally accepted accounting principles.

PricewaterhouseCoopers LLP

PricewaterhouseCoopers LLP
Chartered Accountants

Edmonton, Canada
February 17, 2006

Balance Sheet

As at December 31	2005	2004
	$	$
Assets		
Current assets		
Cash and cash equivalents	10,974,739	2,594,664
Accounts receivable (note 3)	22,621,022	17,432,270
Inventories	9,434,930	5,544,927
Prepaid expenses	144,674	267,178
Current portion of promissory note	122,354	125,964
Current assets of discontinued operations (note 3)	-	2,494,276
	43,297,719	28,459,279
Promissory note	61,186	188,950
Other assets (note 5)	1,475,109	1,397,135
Property, plant and equipment (note 4)	23,037,461	20,252,437
Non-current assets of discontinued operations (note 3)	-	5,305,895
Goodwill (note 1(g))	6,049,530	6,049,530
	73,921,005	61,653,226
Liabilities		
Current liabilities		
Bank indebtedness (note 6)	3,228,132	3,476,944
Accounts payable and accrued liabilities	13,203,125	12,376,288
Income taxes payable	2,097,000	-
Current portion of long-term debt (note 6)	1,215,488	1,173,087
	19,743,745	17,026,319
Long-term debt (note 6)	1,832,276	3,042,634
Asset retirement obligations (note 7)	180,292	169,320
Future income taxes (note 10)	3,940,000	2,208,639
	25,696,313	22,446,912
Contingent liabilities (note 14)		
Shareholders' equity		
Share capital (note 8)	27,973,843	27,465,971
Contributed surplus (note 8(c))	927,199	591,431
Retained earnings	19,323,650	11,148,912
	48,224,692	39,206,314
	73,921,005	61,653,226

Signed on behalf of the Board,

LB Phillips

Larry B. Phillips
Director

Kenneth A. Klein
Director

Statement of Operations and Retained Earnings

For the years ended December 31	2005	2004
	$	$
Revenues	109,132,279	63,619,257
Cost of sales	92,457,554	53,406,748
Gross profit	16,674,725	10,212,509
Expenses		
Salaries and employee benefits	4,892,698	4,237,582
Selling, general and administration	4,864,165	3,342,957
Depreciation and amortization	689,024	1,140,864
Amortization of pre-operating costs	86,871	86,871
Accretion expense (note 7)	10,972	32,059
Interest expense (note 9)	249,918	229,578
	10,793,648	9,069,911
Earnings from continuing operations before other income	5,881,077	1,142,598
Other income		
(Loss) gain on disposal of property, plant and equipment	(24,008)	68,247
Loss on settlement of legal claim	-	(275,344)
Rental and other	80,435	351,008
	56,427	143,911
Earnings from continuing operations before income taxes	5,937,504	1,286,509
Income taxes (note 10)		
Current	1,127,577	-
Future	925,419	526,855
	2,052,996	526,855
Net earnings from continuing operations	3,884,508	759,654
Net earnings from discontinued operations (note 3)	4,290,230	1,201,046
Net earnings for the year	8,174,738	1,960,700
Retained earnings, beginning of year	11,148,912	9,188,212
Retained earnings, end of year	19,323,650	11,148,912
Basic earnings per share (note 8(e))		
Continuing operations	0.26	0.05
Discontinued operations	0.29	0.09
Net earnings	0.55	0.14
Diluted earnings per share (note 8(e))		
Continuing operations	0.26	0.05
Discontinued operations	0.29	0.08
Net earnings	0.55	0.13
Weighted average shares outstanding (note 8(e))		
Basic	14,793,712	14,396,811
Diluted	14,796,030	14,583,232

Statement of Cash Flows

For the years ended December 31	2005	2004
	$	$
Operating activities		
Net earnings from continuing operations	3,884,508	759,654
Items not affecting cash -		
Depreciation, amortization and accretion expense	778,192	1,253,564
Stock based compensation	335,768	293,344
Loss (gain) on disposal of property, plant and equipment	24,008	(68,247)
Future income taxes	925,419	526,855
	5,947,895	2,765,170
Changes in non-cash components of working capital (note 12)	(7,001,837)	(2,234,706)
Net cash flows (used in) provided by continuing operations	(1,053,942)	530,464
Net earnings from discontinued operations (note 3)	4,290,230	1,201,046
Items not affecting cash -		
Depreciation and amortization	791,392	790,109
(Gain) loss on sale of property, plant and equipment	(8,670)	39,199
Gain on sale of specialty chemical operations	(3,746,931)	-
Future income taxes	(400,881)	646,282
	925,140	2,676,636
Net change in non-cash components of working capital	3,186,296	(92,930)
Net cash flows provided by discontinued operations	4,111,436	2,583,706
Net cash provided by operating activities	3,057,494	3,114,170
Investing activities		
Purchase of property, plant and equipment	(3,690,751)	(2,710,114)
Decrease in promissory note	131,374	157,768
Proceeds from disposal of property, plant and equipment	103,360	282,572
Proceeds from sale of specialty chemical operations (note 3)	10,203,817	-
Increase in other assets	(164,845)	(111,299)
Net cash provided by (used in) investing activities, continuing operations	6,582,955	(2,381,073)
Net cash used in investing activities, discontinued operations	(351,477)	(359,955)
Net cash provided by (used in) investing activities	6,231,478	(2,741,028)
Financing activities		
Issuance of common shares	507,872	696,744
Decrease in bank indebtedness	(248,812)	(11,661)
Increase in long-term debt	-	2,260,978
Repayment of long-term debt	(1,167,957)	(864,588)
Repayment of obligations under capital leases	-	(903,515)
Net cash (used in) provided by financing activities	(908,897)	1,177,958
Increase in cash and cash equivalents	8,380,075	1,551,100
Cash and cash equivalents - beginning of year	2,594,664	1,043,564
Cash and cash equivalents - end of year	10,974,739	2,594,664

Supplementary information (note 11)

Notes to Financial Statements
For the years ended December 31, 2005 and 2004

1. Summary of Significant Accounting Policies

(a) Basis of presentation

These financial statements are prepared in accordance with generally accepted accounting principles ("GAAP") in Canada. On December 31, 2005, the Company sold the inventory and property, plant and equipment associated with its specialty chemical operations. Accordingly, the specialty chemical operating activities have been reported as discontinued operations for the comparative years ended December 31, 2005 and 2004. The discontinued operations are more fully described in note 3.

(b) Use of estimates

The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions. The Company bases its estimates on historical experience and on various other assumptions that are believed to be reasonable under the circumstances, the results of which form the basis for making judgments about the carrying values of assets and liabilities that are not readily apparent from other sources. These estimates and assumptions affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

(c) Cash and equivalents

Cash and cash equivalents consist of cash on deposit and short-term interest bearing securities with maturities less than three months.

(d) Inventories

Inventories are carried at the lower of average cost and estimated net realizable value. For finished goods inventory, cost includes direct labour and an allocation of overhead that can be attributed to production.

Effective July 1, 2004, the Company changed its method of allocating feedstock costs to its products and by-products that are produced simultaneously in the same processing operation to the relative sales value method. This change coincides with the establishment of the Energy Marketing segment as described in Note 15. Under this method, joint product costs are allocated based on each products percentage of the total sales value of all products produced. This method results in the same gross profit percentage for each joint or common product produced. Under this method revenues from the sale of the Company's by-products are recorded as revenue with the corresponding cost of by-products sold, as determined under the relative sales value method, recorded as a cost of sales. Prior to this change of method, the net realizable value of by-products were applied as a reduction of the main product processing costs. The adoption of this accounting policy was necessitated by the establishment of the Energy Marketing segment and as such has been applied prospectively.

(e) Property, plant and equipment

Property, plant and equipment are recorded at cost and are depreciated over their estimated useful lives at the following annual rates:

Buildings	5% declining balance
Laboratory equipment	10% declining balance
Land improvements	10% declining balance
Oilfield equipment	10% declining balance
Fractionation processing facilities	straight-line method (described below)
Blend plant facilities	20% declining balance
Leasehold improvements	10% to 20% declining balance
Automotive equipment	30% declining balance
Office, computer equipment and software	20% to 100% declining balance

1. Summary of Significant Accounting Policies (continued)

(e) Property, plant and equipment (continued)

Effective January 1, 2005 the Company changed its estimated useful life of the fractionation processing facilities. Prior to January 1, 2005, the Company depreciated its fractionation plants on a declining balance basis at annual rates ranging from 5% to 10%. Effective January 1, 2005, the Company began to depreciate its fractionation facilities on a straight-line basis which incorporates the change in the plants' expected useful lives which range from 29 to 37 years. The Company has also established estimated salvage values for these facilities based on accepted industry standards. A salvage value of $750,000 has been established for the Slave Lake facility and $250,000 has been established for the Sundre facility. The impact of this change relative to the previous method of depreciation was a reduction in depreciation expense for the year ended December 31, 2005 of $473,172.

(f) Capital leases

Capital leases are capitalized by recording as assets and liabilities the present value of the payments under the leases. The capitalized value of a depreciable asset under a capital lease is amortized over its estimated useful life on a basis that is consistent with the Company's depreciation policy for similar assets. Lease payments are allocated to a reduction of the obligation and interest expense.

(g) Goodwill

Goodwill represents the excess of the cost of business acquisitions over the fair value of net identifiable assets acquired. Goodwill is not amortized but is tested for impairment annually or more frequently if changes in circumstances indicate a potential impairment. Management has performed its annual evaluation of the carrying value of goodwill and concluded that the goodwill associated with its reporting units was not impaired.

(h) Investment in foreign operations

The Company's investment in foreign operations is recorded at cost unless there is a decline in value that is other than temporary.

(i) Future income taxes

Income taxes are calculated using the liability method of accounting. Temporary differences arising from the difference between the tax basis of an asset or liability and its carrying amount on the balance sheet are used to calculate future income tax liabilities or assets. Future income tax liabilities or assets are calculated using tax rates anticipated to apply in periods that the temporary differences are expected to reverse. The effect on future income tax liabilities and assets of a change in the tax rate is recognized in income in the period that the change occurs.

(j) Revenue recognition

Revenues associated with sales of the Company's chemical and hydrocarbon fluids are recorded in the period in which the fluids are delivered to the customer, the customer has taken title, assumed the risks and rewards of ownership, amounts are known and collection is reasonably assured.

(k) Turn around maintenance costs

Effective April 1, 2005, the Company implemented a scheduled turnaround maintenance program for its fractionation plants which requires the shutdown of its facilities for significant overhaul and refurbishment. The Company expects to execute its scheduled turnaround program during the second quarter of each year. Costs of major fractionation plant maintenance are charged to operations over a one year period. At December 31, 2005 unamortized turnaround costs in the amount of $173,520 are included in other assets. For the year ended December 31, 2005, $342,172 of turnaround costs were amortized and included in selling, general and administration expense. Normal repairs and maintenance to the fractionation plants are expensed as incurred.

(l) Earning per share

Basic earnings per common share are calculated based on the average number of common shares outstanding during the year. Diluted earnings per share are calculated based on the treasury stock method which assumes that any proceeds from the exercise of in the money stock options would be used to purchase the company's common shares at the average market price during the year. The computation of diluted earnings per share is similar to basic earnings per share except that the weighted average number of shares outstanding is increased to include additional shares from the assumed exercise of stock options, if dilutive.

1. Summary of Significant Accounting Policies (continued)

(m) Stock based compensation

The Company has adopted the recommendations of the CICA Handbook Section 3870 "Stock Based Compensation and Other Stock Based Payments" which requires the expensing of all stock based compensation awards using a fair value based method of accounting for fiscal years beginning after January 1, 2004. Under the fair value method, compensation expense equal to the fair value of stock options granted is recorded in the statement of operations over the vesting period. The Company's stock based compensation plans are described in note 8.

(n) Pre-operating costs

Pre-operating costs incurred during the start-up of the Company's fractionation plant in Slave Lake, Alberta were capitalized until the plant was capable of consistently providing its intended commercial service. These costs are being amortized over a period of five years which commenced on January 1, 2003.

(o) Incentive plan for senior management

Effective January 1, 2005, the Company implemented an incentive program for designated senior management employees to reward their efforts in acheiving the Company's performance objectives. The term of the plan is for two years ending December 31, 2006. Entitlement to distributions under the incentive plan are subject to the acheivement of corporate objectives as defined by the Company's Board of Directors. During 2005, the corporate goals were not acheived, and as a result, the Company did not incur or accrue incentive payments under the plan.

(p) Asset retirement obligations

The Company adopted the recommendations of the CICA Handbook Section 3110, "Asset Retirement Obligations." This standard requires that obligations associated with the retirement of tangible long-lived assets and associated retirement costs be recognized in the period in which a reasonable estimate of fair value can be made. The standard requires recognition of a liability at a discounted fair value for the future abandonment and restoration associated with the properties. The fair value of the liability is capitalized as part of the cost of the related asset and amortized to expense over its useful life. The liability accretes until the date of expected settlement of the retirement obligation. The related accretion expense is recognized in the statement of operations. The provision will be revised for any changes to timing related to cash flow or undiscounted abandonment costs. Actual expenditures incurred for the purpose of site restoration are charged to the asset retirement obligations to the extent that the liability exists on the balance sheet. Differences between the actual costs incurred and the fair value of the liability recorded are recognized to earnings in the period incurred.

(q) Impairment of long-lived assets

The Company adopted the CICA Handbook Section 3063, "Impairment of Long-lived Assets." A long-lived asset is an asset that does not meet the definition of a current asset. This section requires the Company to test long-lived assets to be held and used when events or changes in circumstances occur which may cause their carrying value to exceed the total undiscounted cash flows expected from their use and eventual disposition. An impairment loss, if any, is determined as the excess of the carrying value of the asset over its fair value. This standard was adopted prospectively on January 1, 2004.

2. Financial instruments

(a) Risk management activities

Concentration of credit risk on the Company's trade accounts receivable exists in the oil and gas industry. Management believes that the Company is exposed to minimal credit risk since the majority of its business is conducted with major companies in the industry.

The Company is exposed to changes in petroleum and natural gas prices as a result of its use of petroleum feedstock and natural gas for processing at its Sundre and Slave Lake fractionation plants. The potential fluctuations in petroleum and natural gas prices could have a significant impact on the cost of producing its products and the profitability of the Company. This risk is reduced in part, from time to time, through the use of crude oil and natural gas forward purchase contracts. The contracts are not used for speculative trading purposes. Realized gains or losses on these contracts are reported as adjustments to petroleum and natural gas costs in the related production period.

The Company did not have any outstanding crude oil and natural gas forward purchase contracts as at December 31, 2005 or December 31, 2004.

2. Financial instruments (continued)

(b) Fair values

The carrying values of cash, accounts receivable, promissory note, accounts payable and accrued liabilities and bank indebtedness approximate their fair value due to the relatively short periods to maturity of these instruments. The fair value of the Company's long term debt is estimated based on market prices for same or similar instruments and approximates carrying value.

(c) Interest rate risk

The Company manages its interest rate risk on borrowings by utilizing a combination of short term fixed rates through the use of 30 to 90 day Bankers' Acceptance rates and floating rates on debt.

3. Discontinued operations

On December 31, 2005, the Company sold the inventory and property, plant and equipment associated with its specialty chemical operations for $13,244,000 of which $826,000 is in accounts receivable at the end of the year. Accounts receivable in the amount of $826,000 represent holdbacks by the purchaser which will be collected on the completion of certain post-closing undertakings by the Company. Subsequent to year end, $250,000 of this amount was collected. The net gain on the sale of the discontinued operations amounted to $3,747,000 after income taxes of $1,484,000. Revenues of $15,789,000 for 2005 and $17,213,000 for 2004 from these discontinued operations are excluded from total revenues in the Statement of Operations.

The balance sheet includes the following amounts related to the discontinued operations:

	2004
	$
Inventories	2,471,398
Prepaid expenses and deferred charges	22,878
Property, plant & equipment	5,305,895

Revenues and operating activities of the specialty chemical operations for the years ended December 31, 2005 and 2004 were as follows:

	2005	2004
	$	$
Revenues	15,789,089	17,213,357
Cost of sales	7,382,896	7,802,274
Gross profit	8,406,193	9,411,083
Expenses		
Salaries and employee benefits	2,905,597	2,979,874
Selling, general and administration	3,796,422	3,627,596
Depreciation and amortization	791,392	790,109
Interest expense	79,425	95,976
Other (income) expense	(1,081)	70,200
Total expenses	7,571,755	7,563,755
Earnings from discontinued operations	834,438	1,847,328
Income taxes	291,139	646,282
Net earnings from discontinued operations	543,299	1,201,046
Net gain on sale of specialty chemical operations	3,746,931	-
Net earnings from discontinued operations	4,290,230	1,201,046

4. Property, plant and equipment

	December 31, 2005			December 31, 2004		
	Cost	Accumulated depreciation	Net	Cost	Accumulated depreciation	Net
	$	$	$	$	$	$
Land	72,859	-	72,859	72,859	-	72,859
Buildings and facilities	1,611,926	404,513	1,207,413	1,335,629	292,238	1,043,391
Laboratory equipment	73,235	10,187	63,048	55,706	12,606	43,100
Oilfield equipment	110,402	53,681	56,721	76,211	48,911	27,300
Fractionation processing facilities	25,534,580	4,074,561	21,460,019	22,209,490	3,505,285	18,704,205
Leasehold improvements	14,137	8,226	5,911	14,137	6,749	7,388
Automotive equipment	746,270	663,564	82,706	1,128,702	888,536	240,166
Office, computer equipment & software	319,465	230,681	88,784	316,931	202,903	114,028
	28,482,874	5,445,413	23,037,461	25,209,665	4,957,228	20,252,437

Buildings and facilities includes $NIL (December 31, 2004 - $81,696) of costs associated with a warehouse and distribution facility under construction in Grande Prairie. Fractionation processing facilities includes $1,246,423

4. Property, plant and equipment (continued)

(December 31, 2004 - $1,640,448) of costs associated with projects under construction at the Slave Lake fractionation plant. Costs associated with these projects have not been depreciated as they have not yet been completed and put in to use.

5. Other assets

	December 31, 2005	December 31, 2004
	$	$
Investments-foreign operations	1,114,442	1,114,442
Pre-operating costs	173,742	260,613
Deferred charges	173,520	-
Other	13,405	22,080
	1,475,109	1,397,135

Investments-foreign operations

Investments-foreign operations represent the Company's investment in its operations in Egypt. During fiscal 1996, the Company entered into an agreement to construct a blend plant in Egypt with Blend Oil Services & Supply. This agreement led to the incorporation of the Egyptian Canadian Company for Chemicals Industries - F.Z., operating in the free zone area of Alexandria, Egypt. The Company has invested $750,000 U.S. ($1,114,442 Cdn.), (December 31, 2004 - $750,000 U.S. ($1,114,442 Cdn.)) maintaining its 25% interest in this Egyptian company. The Company accounts for its investment in this Egyptian Company on the cost basis as it does not exercise significant influence. Earnings from the Company's Egyptian investment will be recognized only to the extent received or receivable. While management believes that the investment in the Egyptian company is fully recoverable, there could be future developments and additional information could become available that may indicate that the carrying value should be revised. Management believes that future revisions to the carrying value, if any, would not have a material adverse affect on the Company's financial condition. However, should such revisions be necessary, the amounts could be material to the results of operations for the period in which they are reported.

Pre-operating costs

Pre-operating costs represent the costs incurred during the start-up of the Company's Slave Lake fractionation plant. The pre-operating period ended January 1, 2003 and the costs are being amortized over a period of five years. At December 31, 2005 accumulated amortization of pre-operating costs is $260,613 (December 31, 2004 - $173,742).

Deferred charges

Deferred charges represent the costs incurred for scheduled turnaround maintenance programs for the Company's fractionation plants. The Company's turnaround maintenance program is described in note 1(k).

6. Bank indebtedness and Long-term debt

	December 31, 2005	December 31, 2004
	$	$
Demand non-revolving loans	3,047,764	4,215,721
Less: current portion of long-term debt	1,215,488	1,173,087
	1,832,276	3,042,634

During 2005, as part of its annual review, the Company renewed its credit facility with a Canadian chartered bank consisting of a $15,000,000 (December 31, 2004 - $15,000,000) demand operating loan that bears interest at the bank's prime rate plus 0.40%; a $1,000,000 (December 31, 2004 - $1,000,000) demand revolving loan at the bank's prime rate plus 0.90%; demand non-revolving loans totaling $5,953,000 (December 31, 2004 - $7,190,000) that bear interest at the bank's prime rate plus 0.90%; and, a $5,000,000 (December 31, 2004 – $5,000,000) bank guarantee facility that bears a fee of 1.35% per annum at the time of issuance of each bank guarantee under the facility. The bank's prime rate at December 31, 2005 was 5.00% (December 31, 2004 – 4.25%). Outstanding non-revolving demand loans are repayable in blended monthly payments of $113,526 (2004 - $113,526) and mature at varying dates from May 2006 to May 2020. At December 31, 2005, the Company had outstanding a demand operating line in the amount of $3,228,132 (December 31, 2004 – $3,476,944).

The Company has pledged an assignment of accounts receivable and inventories, a general security agreement creating a first priority security interest in all present and after acquired personal property of the Company and a floating charge over all of the Company's present and after acquired real property as collateral on its long-term debt and bank indebtedness.

6. Bank indebtedness and Long-term debt (continued)

While the credit facility is demand in nature, repayment of the debt in advance of the agreed terms is not at the bank's discretion provided the Company is not in default of its obligations, covenants and other conditions to the facility that will materially affect the Company's ability to fulfill its obligations. The Company was in compliance with these covenants at December 31, 2005 and 2004.

Approximate principal repayments in each of the next five years are as follows:

	$
2006	1,215,488
2007	415,924
2008	309,277
2009	350,426
2010 and thereafter	756,649

Subsequent to December 31, 2005, the Company repaid the demand non-revolving loans in the amount of $3,047,764.

7. Asset retirement obligations

The Company has recorded the current fair value of its expected cleanup and site closure costs associated with the Slave Lake and Sundre plant locations. The analysis of the asset retirement obligation (ARO) is as follows:

	December 31, 2005	December 31, 2004
	$	$
Asset retirement obligations - beginning of period	169,320	-
Initial ARO on adoption of the new standard	-	137,261
Accretion expense	10,972	32,059
Asset retirement obligations - end of period	180,292	169,320

With the adoption of this standard at December 31, 2004, $137,261 has been included in property, plant and equipment. Included in depreciation and amortization of plant and equipment for the amortization of the ARO is a charge of $3,221 (December 31, 2004 - $39,400) for the year ended December 31, 2005.

The following assumptions were used to estimate the fair values of the obligation on the date the obligation was incurred:

Total undiscounted amount of the estimated cash flows	$1,186,000
Expected timing of payment of cash flows	2033 and 2041
Credit adjusted risk free rate	6.49% and 6.87%

The estimate of the total liability for future asset retirement obligations is subject to change based on amendments to laws and regulations and as new information concerning the Company's operations becomes available. Future changes, if any, to the estimated total liability as a result of amended requirements, laws, regulations and operating assumptions may be significant and would be recognized prospectively as a change in estimate, when applicable.

8. Share capital and Contributed surplus

(a) Authorized -

20,000,000 non-voting, preferred shares, rights to be determined upon issue
Unlimited number of common shares

(b) Issued -

Common

	December 31, 2005		December 31, 2004	
	#	$	#	$
Balance - beginning of period	14,594,610	27,465,971	14,317,655	26,769,227
Issue of shares for cash upon exercise of stock options	150,000	292,500	138,000	272,900
Issue of shares for cash through employee share purchase plan	76,197	215,372	138,955	423,844
Balance - end of period	14,820,807	27,973,843	14,594,610	27,465,971

8. Share capital and Contributed surplus (continued)

(c) Contributed surplus

	December 31, 2005	December 31, 2004
	$	$
Balance - beginning of period	591,431	298,087
Stock based compensation expensed during the period	335,768	293,344
Balance - end of period	927,199	591,431

(d) Stock options

The Company has reserved 2,700,000 common shares for issuance pursuant to an approved stock option plan ("Option Plan") granted to directors and employees of the Company. Stock options granted to employees vest over different periods and amounts from the date of grant and expire five years after the date of grant. The exercise price of each option equals the market price of the Company's common shares at the date of grant. A summary of the status of the Company's Option Plan is presented below:

	December 31, 2005		December 31, 2004	
	Options	Weighted Average Excercise Price	Options	Weighted Average Excercise Price
	#	$	#	$
Common shares under option-beginning of year	1,226,000	3.11	1,214,000	2.94
Share options granted	394,000	3.05	160,000	3.49
Share options cancelled	(434,000)	2.89	(10,000)	5.15
Share options expired	(10,000)	2.70	-	-
Share options exercised	(150,000)	1.95	(138,000)	1.98
Common shares under option-end of year	1,026,000	3.35	1,226,000	3.11
Options exercisable at end of year	517,000	3.52	956,000	2.66

The following options were outstanding and exercisable under the Option Plan at December 31, 2005:

	Outstanding				Exercisable	
		Exercise Price				
Expiry Date	Options	Price	Weighted Average Price	Weighted Average Remaining Years of Contractual Life	Options	Weighted Average Exercise Price
	#	$	$		#	$
April 17, 2006	362,000	3.04	3.04	0.3	362,000	3.04
May 9, 2007	105,000	5.15	5.15	1.4	105,000	5.15
February 11, 2008	15,000	4.00	4.00	2.2	10,000	4.00
August 8, 2008	10,000	3.25	3.25	2.6	5,000	3.25
January 20, 2009	10,000	3.40	3.40	3.1	2,500	3.40
January 20, 2009	100,000	3.40	3.40	3.1	-	-
May 14, 2009	50,000	3.70	3.70	3.4	12,500	3.70
January 4, 2010	354,000	3.05	3.05	4.0	-	-
January 7, 2010	20,000	3.30	3.30	4.0	20,000	3.30
	1,026,000		3.35	2.3	517,000	3.52

8. Share capital and Contributed surplus (continued)

(d) Stock options (continued)

During the year ended December 31, 2005, the Company granted 394,000 options (December 31, 2004 – 160,000) with exercise prices ranging from $2.70 to $3.30 (December 31, 2004 - $3.40 to $3.70). The fair value of the options granted for the year ended December 31, 2005 has been estimated using the Black-Scholes option pricing model. The assumptions used in the pricing model are as follows:

Risk free interest rate (%)	3.72
Expected life of options (years)	5
Expected volatility (%)	51
Dividend yield (%)	0

The impact of expensing the stock options for the year ended December 31, 2005 was $335,768 (December 31, 2004 - $293,344), with a corresponding increase in contributed surplus.

The Company terminated its Employee Share Purchase Plan effective July 1, 2005 and, in place thereof, adopted an employee bonus plan providing for cash compensation based upon the attainment of designated objectives. Under the Company's Employee Share Purchase Plan, employees electing to participate in the plan could contribute a minimum of two percent to a maximum of five percent of monthly salaries. The employees' contributions were matched equally by the Company. Common shares acquired under the plan vested with the employees upon purchase and were distributed to the employees on an annual basis. The Company's contributions to the plan were recorded as compensation costs in the month incurred and totaled $107,686 for the year ended December 31, 2005 (December 31, 2004 - $211,922). During fiscal 2005, 76,197 shares (December 31, 2004 - 138,955) were issued under the plan for proceeds totaling $215,372 (December 31, 2004 - $423,844).

(e) Net earnings per share

Basic earnings per share is calculated using the reported net earnings divided by the weighted average number of common shares outstanding during the period. Diluted earnings per share is calculated on the basis of the weighted average number of common shares outstanding recognizing the effect of outstanding stock options and their equivalent using the treasury stock method.

A reconciliation of the denominators used for the computation of basic and diluted per share are as follows:

	December 31, 2005	December 31, 2004
Weighted average share reconciliation		
- Basic		
Common shares - opening	14,594,610	14,317,655
Weighted average of common shares issued during the period	199,102	79,156
	14,793,712	14,396,811
- Diluted		
Basic weighted average common shares - opening	14,793,712	14,396,811
Dilutive effect of stock options and equivalents	2,318	186,421
	14,796,030	14,583,232

9. Interest expense

Interest expense is comprised as follows:

	December 31, 2005	December 31, 2004
	$	$
Interest on bank indebtedness	131,229	140,954
Other interest	3,760	29,879
Interest on long-term debt	114,929	58,745
	249,918	229,578

10. Income taxes

The following table reconciles income taxes from operations calculated at the combined statutory federal and provincial tax rate with the income tax provision in the financial statements.

	December 31, 2005	December 31, 2004
	$	$
Income taxes based on combined statutory Canadian federal and provincial tax rate	1,996,188	430,296
Substantively enacted rates	-	(37,058)
Non-deductible and other	56,808	133,617
	2,052,996	526,855

	$	$
Cash income taxes paid	-	76,577

Significant components of the Company's future tax liabilities (assets) are as follows:

	December 31, 2005	December 31, 2004
	$	$
Prepaid expenses and deferred charges	62,640	-
Property, plant and equipment	4,023,191	2,879,475
Non-capital losses	-	(497,036)
Other assets	51,541	102,365
Accounts payable and accrued liabilities	(68,363)	(84,050)
Asset retirement obligation	(60,614)	(56,925)
Share issuance costs	(68,395)	(135,190)
	3,940,000	2,208,639

As at December 31, 2005, the Company had non-capital losses available for carry forward of $NIL (December 31, 2004 - $1,478,000).

11. Supplementary cash flow information

	December 31, 2005	December 31, 2004
	$	$
Cash interest income received	62,405	3,687
Cash interest expense paid	329,343	279,383

12. Changes in non-cash components of working capital

Changes in non-cash components of working capital are comprised as follows:

	December 31, 2005	December 31, 2004
	$	$
Accounts receivable	(5,188,752)	(5,541,402)
Inventories and prepaid expenses	(3,767,499)	(1,403,912)
Accounts payable and accrued liabilities	826,837	4,847,830
Income taxes payable	1,127,577	(137,222)
	(7,001,837)	(2,234,706)

13. Commitments

(a) Leases

The future minimum lease payments under operating leases amount to $793,096 (December 31, 2004 - $891,715) and for each of the next five years are:

	$
2006	427,002
2007	137,136
2008	114,479
2009	114,479
2010	-

13. Commitments (continued)

(b) Petroleum feedstock

The Company has entered into contracts of varying terms and quantities for the purchase of petroleum feedstock for processing. These contracts are not speculative.

(c) Chemical purchases

The Company had entered into a two year chemical purchase contract effective December 1, 2003 with a U.S. based private company guaranteeing that the Company would purchase chemicals at market prices in amounts no less than $500,000 U.S. ($600,150 CDN) in each of 2004 and 2005. During 2005, the Company completed its purchase commitment with that supplier.

14. Contingent liabilities

In the normal course of business, the Company is party to various claims and legal proceedings. While the final outcome with respect to the claims and legal proceedings pending, as at December 31, 2005, cannot be determined with certainty, it is the opinion of management that their resolution will not have a material adverse effect on the Company's financial position or results of operations.

15. Segmented information

During 2004, the Company's services were diversified with the establishment of its Energy Marketing Group. This diversification was precipitated to maximize value received by the Company for its hydrocarbon by-products, mitigate the company's exposure to the seasonality of its operations and to provide energy marketing management and expertise. As a result, the Company's activities are divided into two distinct business segments: Oilfield Services which represents the manufacture and sale of hydrocarbon products; and, Energy Marketing which represents the purchasing, gathering and marketing of crude oil for resale to refiners and other customers.

December 31, 2005

	Oilfield Services	Energy Marketing	Total
	$	$	$
Revenues	72,072,308	37,059,971	109,132,279
Cost of Sales	59,577,312	32,880,242	92,457,554
Gross Profit	12,494,996	4,179,729	16,674,725
Depreciation, amortization and accretion expense	786,867	-	786,867
Interest expense	249,918	-	249,918
Other income	56,427	-	56,427
Earnings from operations	2,584,422	3,353,082	5,937,504
Income taxes	925,690	1,127,306	2,052,996
Net earnings	1,658,732	2,225,776	3,884,508
Total Assets	70,476,057	3,444,948	73,921,005
Capital expenditures	3,855,596	-	3,855,596
Goodwill	6,049,530	-	6,049,530

During 2005, the Energy Marketing segment had sales to one customer accounting for approximately 48% (December 31, 2004 - 98%) of total revenues provided by this segment.

15. Segmented information (continued)

December 31, 2004

	Oilfield Services	Energy Marketing	Total
	$	$	$
Revenues	48,667,303	14,951,954	63,619,257
Cost of Sales	39,778,927	13,627,821	53,406,748
Gross Profit	8,888,376	1,324,133	10,212,509
Depreciation, amortization and accretion expense	1,259,794	-	1,259,794
Interest expense	229,578	-	229,578
Other income	143,911	-	143,911
Earnings from operations	285,787	1,000,722	1,286,509
Income taxes	190,414	336,441	526,855
Net earnings	95,373	664,281	759,654
Total Assets	58,799,616	2,853,610	61,653,226
Capital expenditures	2,821,413	-	2,821,413
Goodwill	6,049,530	-	6,049,530

16. Comparative figures

Certain comparative figures have been reclassified to conform with the current year's presentation.

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J. Barrie Brookman
Vice President, Corporate Development (3)

Member of:
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(2) Compensation Committee
(3) Environmental Committee
(4) Strategic Planning and Priorities Committee

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PricewaterhouseCoopers LLP
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Toronto Stock Exchange: trading symbol "ECH"
United States - Over the Counter 12g-3-2(b)

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